

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of)
)
Federal-State Joint Board on Universal Service) CC Docket No. 96-45
)

To: The Federal-State Joint Board on Universal Service

**REPLY COMMENTS OF DOBSON CELLULAR SYSTEMS, INC.
ON CERTAIN OF THE COMMISSION'S RULES RELATING TO
HIGH-COST UNIVERSAL SERVICE SUPPORT**

Dobson Cellular Systems, Inc. ("Dobson") hereby submits its reply comments in response to the Joint Board's *Public Notice* seeking comment on certain rules relating to high-cost universal service support.¹

In its initial comments, Dobson urged the Joint Board to take note of the evolving telecommunications marketplace and recommend rules and policies that will reflect and accommodate the significant changes in how rural consumers utilize telecommunications services. The deployment of advanced and new technologies and the ever-increasing level of competition require a forward-looking approach to a universal service system that has for far too long been based on monopoly-era policies. Consumers are the true winners in this rapidly advancing telecommunications marketplace and also must be the true beneficiaries of properly targeted universal service support. This is the only way to ensure that all consumers, particularly those in rural areas, enjoy the benefits of advanced communications capabilities.

Many commenters recognized this new reality and the need to tailor universal service policies to meet the changing environment. Commenters also agreed with Dobson that the Joint

¹ *Federal-State Joint Board on Universal Service Seeks Comment on Certain of the Commission's Rules Relating to High-Cost Universal Service Support*, CC Docket 96-45, *Public Notice*, FCC 04J-2 (rel. Aug. 16, 2004) ("Public Notice").

Board must focus its attention on reforming the amount and manner by which ILECs receive support in a way that takes into account the unmistakable presence and benefits of competition. In this reply, Dobson focuses on certain discrete issues raised in the initial comments.

DISCUSSION

I. THE DEFINITION OF “RURAL” MUST BE CHANGED.

As noted in the *Public Notice*² and necessarily acknowledged even by the rural telco community,³ use of the statute’s definition of “rural telephone company” is inappropriate for determining eligibility for embedded, cost-based high-cost support.⁴

As an initial matter, Dobson reiterates that transitioning *all* carriers to a support mechanism based on a forward-looking cost model is the best long-term solution for ensuring needed efficiency and competitive neutrality in the funding mechanism.⁵ Nevertheless, Dobson understands that a certain amount of time and effort may be required in order to develop a model that can be applied to carriers that have more complex and idiosyncratic cost characteristics than those who receive support based on the existing model. Thus, there remains a short-term need to continue to identify “rural carriers” that should receive support based on embedded costs. As noted above, however, the statutory definition of “rural telephone companies” is inappropriate to this purpose.

Dobson believes that an appropriate definition of “rural” for this purpose will focus on identifying areas that are, in fact, difficult to model. There is no evidence that the definition

² *Public Notice* at ¶ 9.

³ See Coalition of State Telecommunications Associations and Rural Telephone Companies Comments at 6; Rural Independent Competitive Alliance Comments at 7-8; Fred Williamson and Associates, Inc. (“FW&A”) Comments at 3-4.

⁴ See Dobson Cellular Systems, Inc. (“Dobson”) Comments at 4-6; Western Wireless Corporation (“Western Wireless”) Comments at 32-34; Surewest Communications Comments at 2-5.

⁵ See Dobson Comments at 6-8; *see also infra* Section II.

currently used (the statutory definition of rural telephone companies) is in any way suited to this purpose. Instead, the record in this proceeding strongly suggests that low population density is a key indicator, yet it is not a component of the statutory definition.⁶ Further, the definition in the statute is difficult to apply given the ambiguity in the term “communities” as used in the statute.⁷

Accordingly, as an interim measure, the Joint Board should recommend that “rural” carriers (*i.e.*, those that will continue to receive embedded-cost support) should be identified based on population density as measured over a geographic area with clearly defined boundaries. Basing a definition of “rural” on population density, combined with selecting an easily recognized geographic area (such as a U.S. Census Bureau “urbanized area”), would provide carriers with a clear and verifiable standard that could be implemented simply. Furthermore, a bright-line density threshold, such as 100 persons or less per square mile,⁸ or those areas lying outside of the U.S. Census Bureau’s “urbanized areas,” would be easy to administer and would accurately capture carriers with cost characteristics that are not susceptible to accurate estimation by the existing universal service cost model.

Predictably, the rural telcos that benefit from the current definition support retention of the status quo. Some oppose any change out of concerns about a potential reduction in their support or because they claim a change to the definition would have little effect on controlling

⁶ See FW&A Comments at 4-5 (“The key driver of high costs of providing services is the population density of the area served. ... population density can be used as a key indicator of whether the areas served by an ETC are rural and high cost areas for purposes of determining universal service support.”); *see also* ALLTEL Corporation Comments at 5; Frontier and Citizens ILECS (“Frontier and Citizens”) Comments at 5.

⁷ See Dobson Comments at 5-6; Western Wireless Comments at 32-34.

⁸ Such a threshold would be consistent with prior FCC analysis for purposing of defining “rural” in order to promote wireless service to rural areas. *See Facilitating the Provision of Spectrum-Based Services to Rural Areas and Promoting Opportunities for Rural Telephone Companies To Provide Spectrum-Based Services*, WT Docket No. 02-381, *Report and Order*, 19 FCC Rcd 19078, at ¶¶ 10-12 (2004); *see also* FW&A Comments at 6-7.

the growth of the fund.⁹ Given the economic efficiency inherent in the use of an objective measure of cost, however, like a model, the purpose of any definition must be to properly identify the universe of carriers whose costs truly cannot be estimated accurately with current economic models.

Another issue that the definition of “rural” must address is the inclusion of all of a carrier’s lines in a state – not just those within an arbitrary “study area.”¹⁰ In initial comments, Dobson and other parties observed that holding company size, rather than study area size, should be considered in determining whether a carrier is “rural” for universal service purposes.¹¹ As these commenters point out, and the Joint Board itself acknowledges, it is difficult to explain why holding companies serving hundreds of thousands of lines within a state are categorized as rural, while other, much smaller carriers – sometimes even in the same state – are not.

Rural ILECs’ claims that the study area should continue to be used because non-contiguous service areas lack economies of scale are self-serving. The availability of fiber-optic transport facilities largely has erased the significance of distance in telecommunications networks. There is no reason that an ILEC could not achieve virtually the same economies of scale with multiple, non-contiguous exchanges as with multiple contiguous exchanges.

Similarly, rural ILECs’ threats that use of statewide averaging would merely spark a rash of corporate reorganizations are refreshingly frank, given many of these carriers’ success thus far

⁹ See Organization for the Promotion and Advancement of Small Telecommunications Companies Comments at 5; United States Telecom Association Comments at 7.

¹⁰ See Dobson Comments at 5.

¹¹ See, e.g., Dobson Comments at 4-5; Verizon Comments at 5; *see also* CTIA-The Wireless Association (“CTIA”) Comments at 8-9; Nextel Communications, Inc. (“Nextel”) Comments at 11, 15-16.

under the current system.¹² Yet there is no reason to believe that the Joint Board and the Commission could not formulate safeguards against the effects of gaming. The Commission's current rules relating to the amount of support available on the sale of exchanges are effective.¹³

A similar approach could be followed here.

II. THE RAPIDLY EVOLVING TELECOMMUNICATIONS INDUSTRY REQUIRES A TRANSITION TO A FORWARD-LOOKING MECHANISM FOR "RURAL" AREAS.

Many commenters support a transition to a forward-looking cost mechanism for all high-cost USF recipients. Forward-looking mechanisms have long been recognized by the FCC as the best way to set prices in competitive markets.¹⁴ The rural carriers themselves have recognized that rural markets are "ripe for competition."¹⁵ If such is the case – and it is, as evidenced by the increased build-out in rural areas by local, regional and national wireless carriers – the Commission should continue to foster such competition by beginning the transition for rural LECs to a forward-looking mechanism.

Use of the FCC's embedded high-cost support mechanism, on the other hand, "create[s] incentives and opportunities for carriers to have higher embedded costs to receive more support."¹⁶ Carriers using embedded cost mechanisms are discouraged from taking advantage of

¹² See, e.g., CenturyTel, Inc. Comments at 15; Frontier and Citizens Comments at 3; ACS of Alaska, Inc. Comments at 6. Indeed, some commenters in this proceeding, such as GVNW Consulting, Inc. and John Staurulakis, Inc., are consulting firms that specialize in helping ILECs maximize their USF support.

¹³ See 47 C.F.R. § 54.305.

¹⁴ See, e.g., Western Wireless Comments at 19 (quoting *Review of the Commission's Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Services by Incumbent Local Exchange Carriers*, WC Docket No. 03-173, *Notice of Proposed Rulemaking*, 18 FCC Rcd 18945, 18957-58 (2003)).

¹⁵ Independent Telephone and Telecommunications Alliance ("ITTA") Comments at 16.

¹⁶ CTIA Comments at 7.

economies of scale.¹⁷ In fact, the only carriers that argue in favor of continued use of the embedded cost mechanism are those who stand to benefit from these monopoly-era regulations that ensure an above-market return on all investment, irrespective of whether expenses are prudently incurred.

One of the primary arguments made by the rural LECs is that “[t]he Commission has never been able to identify a model that can reliably predict costs in rural markets.”¹⁸ Such an argument is obviously self-serving; with enough time and effort, a model can be developed. In fact, the Commission has never tried to create such a model. Because computing support for all carriers using a forward-looking mechanism would more appropriately compute universal service support for the benefit of consumers located in high-cost areas, and for all consumers who share the burden of the increasing universal service fund, the Joint Board cannot accept such a rush to judgment.

From the release of the *First Universal Service Report and Order* in 1997, the Commission always has had the intention of creating a forward-looking cost model for rural carriers.¹⁹ At that time, the Commission stated that a forward-looking model “should be able to predict rural carriers’ forward-looking economic cost with sufficient accuracy that carriers serving rural areas could continue to make infrastructure improvements and charge affordable rates.”²⁰ Moreover, the Commission noted the benefits that the use of a forward-looking

¹⁷ CTIA Comments at 7-8; *see also* CTIA Comments at ii (“The [FCC’s] high-cost universal service mechanisms are one of the few remaining remnants of a pre-divestiture regulatory structure designed to guarantee profits to inefficient monopolies insulated from competition.”).

¹⁸ ITTA Comments at 23. FairPoint Communications, Inc. (“FairPoint”) also stated that it was difficult, if not impossible, to fix the Synthesis Model. FairPoint Comments at 13. The rural carriers seem to reject outright any effort to change the model before any such effort even is undertaken.

¹⁹ *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *Report and Order*, 12 FCC Rcd 8776 (1997) (“*First Report and Order*”).

²⁰ *Id.* at 8935.

mechanism would bring to rural areas, stating that “incorporating forward-looking economic cost principles would promote competition in rural study areas by providing more accurate investment signals to potential competitors.”²¹ In fact, the Commission stated in 1997 that it anticipated a forward-looking mechanism for rural carriers with sufficient accuracy would “be developed within three years of release of this Order.”²²

Certainly by 2005 rural carriers must begin accepting the reality of competition, that already has been years in the making, and the need for related adjustments to the universal service program. Even in 1997, the Commission recognized the value of forward-looking cost methodologies to the developing competition in the telecommunications industry:

[W]e find that, rather than causing rural economies to decline, as some commenters contend, the use of such a forward-looking economic cost methodology could bring greater economic opportunities to rural areas by encouraging competitive entry and the provision of new services as well as supporting the provision of designated services. Because support will be calculated and then distributed in predictable and consistent amounts, such a forward-looking economic cost methodology would compel carriers to be more disciplined in planning their investment decisions.²³

It is time for the Joint Board to recommend the development of a forward-looking cost mechanism for rural carriers to proceed without further delay.

Dobson and the other commenters that support a transition to a pro-competitive, forward-looking mechanism appreciate the need for an investment of time and resources in order to develop an accurate and reliable rural mechanism. Moreover, Dobson supports the use of safety valves and a transition period that will allow rural LECs to maintain reasonable funding levels

²¹ *Id.* at 8936.

²² *Id.* at 8935.

²³ *Id.* at 8936 (citations omitted).

for a fixed period of time.²⁴ Despite the effort that may be required to create a reliable forward-looking rural mechanism, *it must be undertaken* because of the benefits that consumers will experience from use of a model for calculating universal service support.

Several companies have made proposals about how the Commission can begin transitioning rural carriers to a forward-looking mechanism.²⁵ Over a year ago, Western Wireless submitted an economic analysis that outlines steps that would have to be addressed to create a workable rural forward-looking cost model.²⁶ Nextel Partners recommends that the Commission create a new rural task force with membership from both wireline and wireless ETCs that would make recommendations on a long-term, forward-looking high-cost methodology based on both wireline and wireless models.²⁷ Dobson would support the establishment of a new rural task force to consider Western Wireless' and others' proposals for moving forward with creation of a forward-looking mechanism. The Joint Board and the Commission must – at the very least – insist on attempting to create a reliable forward-looking rural mechanism in keeping with the Commission's goals of competition and deregulation.

²⁴ The Commission foresaw the need for a transition period in the *First Report and Order*: “Rural carriers will shift gradually to a forward-looking economic cost methodology to allow them ample time to adjust to any changes in the support calculation.” *Id.* Western Wireless also supports the use of a safety net for rural carriers, stating that there should be a cap on the yearly percentage reduction in support. Western Wireless Comments at 34-36.

²⁵ See, e.g., Western Wireless Comments at 21-28 (proposing three options for determining forward-looking costs: (1) use the Synthesis Model or an alternative with modified inputs, (2) develop estimates based on existing plant accounts, apply adjustments to update the booked costs to reflect intervening cost trends, benchmark operating expenses and corporate overhead costs using a “best in class” model, and make other modifications that reflect the routing and topography of an ILEC’s existing facilities; or (3) over the long term, compare ILEC forward-looking estimates with estimates generated from a wireless-specific model to determine the least-cost technology); Sandwich Isles Communications, Inc. Comments at 16 (stating that if a forward-looking mechanism is to be used, it should be determined based on a company-specific study); Sprint Corporation Comments at 3-4 (stating that the FCC should “initiate a process to move toward forward-looking costs by benchmarking the average costs incurred by rural rate of return ILECs against those incurred by similarly-sized, similarly-situated rural price cap ILECs”).

²⁶ See Western Wireless Comments at 24 and Exhibit 5.

²⁷ Nextel Partners, Inc. (“Nextel Partners”) Comments at 9-10.

III. THE JOINT BOARD SHOULD REJECT THE RLECS' CLAIM THAT INVESTMENT IN RURAL NETWORKS WILL BE UNDERMINED BY ANY REGULATORY CHANGE THAT MIGHT REDUCE THE RLECS' SUPPORT.

The rural carriers are very quick to dismiss any form of regulatory change, automatically asserting that any change will reduce support and hamper investment in rural areas. Not only is this speculative, it fails to acknowledge that the Act was promulgated to promote competition, not to protect competitors, and that the universal service program is intended to benefit consumers, not providers.²⁸

The rural carriers also assume that their investors should face no uncertainty about their returns. The rural LECs believe that even debating the merits of transitioning to a new mechanism will lead to uncertainty and limit investment. Yes, competition has risks. But that has not stopped the flow of outside funding in virtually every other telecommunications market. Wireless carriers have invested hundreds of millions of dollars to deploy advanced wireless networks capable of supporting high-speed data applications, including into high-cost areas. While some of these wireless carriers recently have begun receiving universal service support, all of them operate in a highly competitive market under a regulatory regime that guarantees them no assured return on investment. The Joint Board must look to the unstoppable competition that is entering rural areas and plan for the future.

Moreover, the objective of universal service is to bring modern, state-of-the-art communication and information services to consumers living in rural areas, not just to perpetuate

²⁸ General Communications, Inc. ("GCI") Comments at ii ("To be consistent with Congress' fundamental, pro-consumer focus, GCI recommends that the Joint Board and the Commission follow three, inter-related principles. First, universal service programs for rural, insular and high cost areas must create incentives for the deployment of rural infrastructure. Second, to the extent possible, the incentives to develop rural infrastructure should be market drive[n], not centrally planned. In other words, universal service support should be harmonized with the Telecommunications Act of 1996's pro-competitive goals. Third, universal service support must be sustainable.").

existing incumbent services.²⁹ Perpetuating universal service policies that shield historical monopolists in rural areas from competition will not bring about these important changes. As General Communications, Inc. noted, the history of service provided by monopolies in Alaska demonstrates that rural consumers get only as much as the monopolist chooses to deliver.³⁰ “When competition is possible, the net result is that rural consumers will receive better service at a lower price.”³¹ The Joint Board should reject claims that regulatory change for the rural LECs will harm rural consumers; only if competition is thwarted will consumers be harmed.

CONCLUSION

Ample evidence has been provided to the Joint Board to justify rejecting the rural LECs’ claims that the status quo should be maintained. Competition has come to the rural markets, and it is the responsibility of the Joint Board and the Commission to foster such competition by effectuating the appropriate changes in the definition of a “rural telephone company” and in the high-cost support mechanism.

Respectfully submitted,

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²⁹ Nextel Partners Comments at 6.

³⁰ GCI Comments at 9.

³¹ *Id.* at 7.

CERTIFICATE OF SERVICE

I, Patrice Wilson, hereby certify that true and correct copies of the foregoing “REPLY COMMENTS OF DOBSON CELLULAR SYSTEMS, INC. ON CERTAIN OF THE COMMISSION’S RULES RELATING TO HIGH-COST UNIVERSAL SERVICE SUPPORT” have been served this 14th day of December, 2004, by United States mail, first class postage prepaid or via electronic transmission upon the following:

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